



British Airways plc,
Waterside,
PO Box 365,
Harmondsworth,
UB7 0GA

Mr. Laurence Crook, Programme Director NR28
Consumer and Markets,
CAA – Civil Aviation Authority,
11 Westferry Circus, Canary Wharf,
London, E14 4HD, UK
e-mail: economicregulation@caa.co.uk

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British Airways response to CAP3190
“NR28 price review: draft method statement and business planning guidance”

Dear Laurence,

Thank you for the opportunity to respond to CAP3190 “NR28 price review: draft method statement and business planning guidance”. We set out below our views and areas of feedback.

This submission is provided in addition to, and not in place of, the fuller airline community response. The fact that we do not repeat specific points from the community submission should not be taken to imply any lack of support for them. Rather, this response focuses on a selected number of additional points specific to British Airways, without prejudice to the collective positions.

1. Priorities and Consumer Research

- 1.1. We support the CAA’s recognition that **safety remains its primary duty** in the discharge of its duties in regards to NERL. Safety is our highest priority, forming an unquestionable predominant priority that should be at the heart of NERL’s business. NERL forms a critical partner in delivering, and the management of, a safe aviation system which is dependent on the interaction of numerous stakeholders, and we support NERL in its efforts and recognise its achievements in delivering the level of safety demonstrated.

- 1.2. It is our belief that NERL should continue furthering safety standards and build upon its expertise and approach to safety during the NR28 period, enhancing its collaboration with and understanding of the various stakeholders engaged in the delivery of a safe operating environment to continue to refine its understanding and representation of risk. Numerous developments including, without limitation, Airspace Modernisation, new airspace users (authorised or otherwise) as well as any repeat of GPS interference form emergent or evolving risks during the upcoming price control period. NERL’s role forms a foundational keystone in the determination and management of these risks.



- 1.3. We support CAA intent and outline areas to **take account of the Egis, Halliwell and 2024 Reviews** in establishing priority areas and points of assessment in establishing the NR28 price control.
- 1.4. We **agree with the CAA's outlined priorities but hold a number of additional areas and points of concern** that we encourage the CAA to consider and take into account in its Final Method Statement.
- 1.5. **Modernising the UK's airspace** is critical to supporting economic growth, reducing delays, and improving environmental performance. There is a clear and compelling need for the entire UK network system to be modernised to deliver the transformative change that is required to enable UK airspace to meet the challenges of increased traffic in the 21st century. Without urgent reform, delays are forecast to worsen significantly, with a greater than five-fold increase to delays resulting from a 28% increase to traffic in the LTMA by 2040¹, threatening consumer experience and the wider economy. The modernisation of the LTMA airspace, through a singular design, is a critical prerequisite to expansion at London Heathrow and is further heightened in importance when other London airport expansion plans are considered for their effects on traffic growth within the LTMA.
- 1.6. There should be greater focus on enabling the sector to work together to achieve sustainability outcomes. This is to be achieved by enabling users to meet their net zero targets by reducing emissions and waste, such as through operational improvements, improved flight efficiency and enhanced resilience. A key enabler in this regard is the delivery of airspace modernisation, particularly in the Lower airspace and terminal manoeuvring areas, with NERL positioned as the fundamental enabler and delivery point in both its obligations under the UKADS as well as the essential developments to its technological systems and processes. Improving flight path efficiency is critically important in our endeavours to achieve aviation's environmental targets through reducing net emissions and ensuring operations are more sustainable.
- 1.7. To support and guide the programme of works associated to the delivery of modernised airspace in the LTMA by 2035, the CAA needs to establish a **clear requirement for NERL to provide an explicitly defined, detailed strategic roadmap for ATM deliveries over the next 10 years to the delivery of the Common Platform and realisation of Airspace Modernisation at least in the LTMA**, as UKADS' first obligation. A strategic roadmap will frame the requirements necessary to be achieved during NR28, and should set out options with calculated trade-offs for their effects, enabling the appropriate establishment of objective deliveries, associated allowances and calibrated decisions across building blocks for the NR28 regulatory settlement. In support of the critical nature of deliveries in the NR28 period, we consider that **addressing NERL's timely and efficient delivery of capital programmes, including an appropriate incentive framework, should be reflected by the CAA as priority for NR28**.

¹ <https://www.caa.co.uk/publication/download/19383>



- 1.8. Over the next decade, there is a material risk that airport growth plans progress ahead of proven, deliverable airspace capacity. This would drive disproportionate increases in delay, undermine network resilience and ultimately worsen passenger outcomes. **We do not accept that deterioration in service is an inevitable consequence of the transition required.** NERL should identify the specific areas and periods where there is risk to service performance and set out mitigating options for assessment.
- 1.9. It is our view that **service performance should not be allowed to unduly diminish from the levels presented in NR23 to date, service outages aside**, and any service targets should be calibrated to building block allowances and cost elements which should be transparently evidenced in detail to allow robust scrutiny and assessment by stakeholders. At its core, NERL should ensure the provision of appropriate capacity as required by traffic without generating undue, excessive delay or negative environmental implications.
- 1.10. We are concerned that the CAA's reference to reflecting the needs of users and consumers appears to be limited solely to the regulation of NERL's service quality. It is our firm belief that the CAA should take account of user and consumer needs to cover all building blocks. **Further guidance is required from the CAA to address how it intends to rank and weight the varying priorities presented by users, consumers and other stakeholders** where differences could emerge.
- 1.11. **The CAA's consideration of affordability appears limited despite its clear relevance as one of the CAA's secondary duties.** Establishing a desired balance between service performance, capex deliveries and opex costs against traffic forecast and financial parameters needs to be considered within the bounds of affordability and should be encouraged as a top-down check presented consistently in options assessment during Constructive Engagement, NERL's Business Plan and subsequently the CAA's assessment and determination.

2. Cost Assessment

- 2.1. Addressing the high-cost base and ensuring efficient charges should be a primary policy driver. NR28 requires a stronger discipline embedded from the outset in BP Guidance and in the CAA's cost assessment plan — **ensuring that cost allowances are earned through evidence and that investment is demonstrably linked to user-relevant outcomes.**
- 2.2. We support the CAA's intent to **widen its evidence base and adopt an enhanced cost assessment approach, especially the use of rigorous bottom-up cost assessments** for material elements of NERL's opex and capex, as well as cost elements facing proposed significant cost increases.
- 2.3. We **have significant concerns about reliance on top-down benchmarking.** Benchmarking must be used carefully, transparently, be well defined for its objective and methodology,

and only where comparability is robust and stakeholders can interrogate underlying data and adjustments. Benchmarking methodology must be carefully designed and take account of local variances with clearly defined assumptions and adjustments. There should be no assumption that peer ANSPs are effectively regulated or provide a reference point of efficiently delivered outputs.

- 2.4. We suggest that the Final Method Statement **places a strong requirement on NERL to provide an explicit and consistently evident “golden thread” for cost elements**, options and proposals that demonstrates the links and calibration for their effects to other building blocks, in particular across; service performance, opex and capex. In its presentation of options and proposals, they must clearly link to consumer and user priorities, illustrating and quantifying how the cost element supports the priorities and any trade-offs associated to it. We consider it would present best practice for this demonstration to be adopted by the CAA as well in setting forward its own assessments and determination.
- 2.5. We encourage the CAA to ensure that only efficient and sufficiently evidenced and justified costs are allowed. **If NERL does not present sufficient justification for cost elements the CAA must be prepared to exclude the costs from its determination of NERL’s cost allowances.** This is beyond the potential application of any Business Plan Incentive, and is a direct disallowance of unjustified costs from the building blocks. Information should be shared consistently and transparently with stakeholders as well as the CAA to allow transparent scrutiny and address information asymmetry.
- 2.6. The CAA should **pursue the revelation of the efficient point of cost occurrence that provides the delivery of the required outputs.** There should be a clear identification and recognition of efficiency gains over time, and allowances should reflect an incentive on NERL to pursue further efficiency realisation akin to the pressures experienced by a commercial entity in a competitive market. In our own business, we are **driven to achieve efficiency gains that at least offset inflationary effects and present reductions in our costs on a repeated, annual basis.** We would support the CAA reviewing inflationary effects on NERL’s costs to determine if blanket inflationary adjustments remain appropriate and do not present the opportunity for windfall gains or losses to arise.

3. Regulatory Framework

- 3.1. We **present unequivocal support for the use of an independent traffic forecast for the purpose of setting the regulatory settlement.** STATFOR appears to represent the continuing, most appropriate forecast for setting NERL’s En Route and London Approach frameworks. We appreciate NERL’s considerations and accuracy cross checks against its own internal traffic forecasting sources and their ongoing efforts to input and support the robustness of STATFOR’s traffic forecasting methodology, which we advocate should be done in conjunction with the regulator and industry to best support the delivery of an appropriate and optimal output. We note the level of assurance that could be gained from the high level and initial oversight of the NATS derived forecast presented in CE1 against



the STATFOR Base Case for IFR movements across the NR28 time period, with NATS confirming in CE1 the use of IFR to determine core operational requirements in its business planning cycle.

- 3.2. We are clear and unwavering in our advocacy for the use of an independent traffic forecast and consider STATFOR presents the most appropriate source. We **encourage cross checks against other indicators and forecasts to ascertain that the STATFOR Base Case presents the most appropriate scenario for the core planning of NERL's NR28 Business Plan.**
- 3.3. We note the CAA's assertion that traffic forecasts hold considerably less uncertainty than those presented for NR23. As such we **consider the CAA should review the traffic modulation and traffic risk sharing mechanisms that are in place**, especially those that were introduced or adjusted for NR23, to ensure their calibration and presence remains appropriate under the expectations of NR28.
- 3.4. We are **concerned at the level of scrutiny proposed to address the approach to Oceanic traffic forecasting** for Shanwick and Tango regions. We consider it appropriate that both NATS' methodology and forecast accuracy for these areas is reviewed to ensure the approach is appropriate and presents an optimal solution for NR28. We are concerned at the reliance on a traffic forecast derived by the regulated entity. We **note the presence of an updated independent, industry forecasts for Oceanic traffic in the form of the ICAO EFFF**, which was lacking for the NR23 price control review. We note that it might not be proportionate to establish a CAA appointed independent traffic forecast for this element of NERL's business, a point that should be clarified for its associated costs, but we do encourage the CAA to consider Oceanic traffic forecasts, both for Shanwick and Tango regions, as a point of assessment for establishing its price control determination for NR28.
- 3.5. We **advocate for the adoption of a determined cost approach for UKADS and UKACS for NR28, with appropriate efficiency incentives to be incorporated.** The establishment of an efficient cost allowance should be informed by improved certainty on delivery obligations as well as policy requirements and processes such as CAP1616 developments.
- 3.6. Clear lineation of cost apportionment for airspace deliveries is required between NERL's business units including its En Route and, or London Approach capex costs and those incurred and attributed to its UKADS or UKACS units. An example of such instance that could require attention is the apportionment of airspace design deployment costs and whether these fall under the SIP as an Operational Service Performance Enhancement or if these are attributable to UKADS/UKACS. The CAA should ensure there is no scope for duplication of costs and charges to consumers from related activities.
- 3.7. It may be appropriate for the associated costs of airspace modernisation to be reconciled via a RAB based model considering the balance of cost to benefit realisation between current and future consumers. We advocate for further dialogue and consideration to be



made with stakeholders on the cost approach for UKADS and UKACS in NR28 as part of the round.

4. Financial Framework and Risk

- 4.1. We urge the CAA to establish an appropriate reflection of the critical essence that insulating NERL from all eventualities is inconsistent with the risk of a regulated business. **We hold significant concerns about the overall balance of risk and reward in the regulatory framework, particularly regarding volume risk.** The current framework includes several layers of protection for NERL against volume risk, not limited to the calibration of the traffic risk sharing (TRS) mechanism, which itself while appearing balanced on paper, effectively provides NERL with disproportionate protection. The TRS mechanism's banding structure, combined with the typical pattern of traffic shocks (sharp, short-term downside events versus gradual upside growth), means NERL receives greater downside protection in aggregate.
- 4.2. In the consideration of accounting for future significant traffic shock events in its design of the TRS mechanism, **the CAA should be conscious of the reflection of such risks in market estimates of risks and their reflection in any appropriate betas, with market estimates of risk providing a considered robust approach.** The CAA should be mindful of creating duplicative adjustments, notably for considerations that should already be captured in the asset beta and, or the calibration of incentives.
- 4.3. We are **cautious on the merits of introducing a TRS mechanism for Oceanic**, it is unclear as to the developments since the review of this area for NR23 and as such currently hold a consistent position in this regard. We are open to exploring a case for this to be reviewed for NR28 but any proposal would need to clearly address its implications on the complexity and proportionality of regulation to the level of consumer benefit anticipated.
- 4.4. **We do not believe the NR23 WACC methodology should be retained without review.** We strongly advocate for the points raised in the joint airline response regarding the approach to the WACC for NR28.
- 4.5. **We request the CAA provides differing WACC values to reflect any adjustments to risk-sharing mechanisms to allow appropriate and transparent assessment by stakeholders** if adjustments are in user and consumers best interests.
- 4.6. **We support the replacement of RPI with CPI**, considering this is overdue. In reviewing its approach to the measure of indexation we would advocate that the CAA review the various applications and adjustments made for inflation within its price control model to ensure any accounting for differences between forecast and actual inflation are addressed and remain appropriately designed. Furthermore, we encourage the CAA to ensure its inflationary allowances and mechanisms remain appropriate and do not present opportunity for windfall gains by NERL. The CAA should clearly set out its pass-through

logic and comparison data in any indexation allowance against treatment in competitive entities.

- 4.7. As part of its assessment of inflationary effects and any appropriate inflation measure to adopt, and adjustments required as a result to price control mechanisms, **we request that the CAA provides a WACC estimate for NERL to apply, for both proposed indexation measures, during the CE process and in its BP.**
- 4.8. The rate of depreciation should be reflective of the period of use of the assets and extent of their economic value that construct the RAB. We request the CAA provides a breakdown of the content of the opening RAB and the asset life projections for new assets entering the RAB during NR28, with an assessment of a representative depreciation period to affirm the appropriate approach. We consider this a particular relevant area for NR28 due to the level of proposed investment in the period, the delivery of significant technological transformation programmes providing significant new assets and the extended lifespan demonstrated by systems such as NAS.

5. Service Performance and the Incentives Framework

- 5.1. **We support that service performance metrics should be comprehensively reviewed during the NR28 price control process for capacity and environmental outcomes.** There should be a comprehensive review supported by deep dive analysis of NERL's performance from the start of RP2. This should be considered in context of their links to user and consumer outcomes, mindful of the representation that user requirements present pseudo presentation of the needs of their customers as end consumers of their services.
- 5.2. NR28 offers an **opportunity to consider whether the performance framework adequately reflects the priorities and real impact points to users and consumers.** Moreover, both a more granular lens - ensuring localised issues are not masked by aggregated data - and a holistic recognition of the end-to-end ATM system, (e.g. flow management, runway throughput, airborne holding and start-up delay), should all be considered to **ensure that performance is measured in a way that meaningfully captures the drivers of service quality and supports a more accurate understanding of operational outcomes.**
- 5.3. The consideration of **capex incentives needs to extend to incentivising the cost efficient and timely delivery** of NERL's capex programmes. We support the consideration of ex-ante capex efficiency incentives, and the assessment for a stronger approach to promote efficiency in capital spending and delivering projects with firm and measurable objectives and costs.
- 5.4. The capex engagement incentive is supported but should develop as part of any changes to NERL's capital incentive framework to ensure it remains complimentary of any additional incentives. The engagement incentive as a minimum should be strengthened to provide greater voice for users in the prioritisation and decision making on NERL's investment plan.



It should also refine the expectations on the extent and quality of information required from NERL to further encourage improvements to NERL's optioneering and consistent quality of information to require cross-functional and outcome costs and benefits such as cross-project or programme, opex and service performance effects of options.

6. BP Guidance

- 6.1. We support that NERL should prepare a base scenario, which should be calibrated to an appropriate STATFOR scenario based on forecast cross checks, and this should be supplemented with scenario analysis. This scenario analysis should extend beyond traffic forecast cases and should incorporate any potential changes to material assumptions in NERL's plans such as changes to airspace modernisation obligations or programme delays and, or scope adjustments to its major technological transformation programmes as well as significant shifts in financial parameters such as inflation. This will best support optioneering to be presented by NERL during Constructive Engagement, which should be supported by further guidance.
- 6.2. We **advocate for the CAA to strengthen its guidance provisions on the need for NERL to present justified and calibrated cost elements as options for consideration by users during Constructive Engagement, with a clear provision of information demonstrating the "golden thread"** of cross building block and outcomes implications of options as well as any associated trade-offs required.
- 6.3. The inputs and preferences from users and how cost elements deliver on user and consumer priorities should be specifically reflected in NERL's BP.
- 6.4. We recognise the need to improve NERL's BP quality, given NR23 experience. However, we do not support rewarding NERL for meeting regulatory obligations. It is inappropriate for a regulated entity to earn incremental income for delivering an activity that is fundamental and expected within the context of a price control. We therefore **recommend that any BP incentive should be penalty-only and set a consistent, very high bar with stringent evidence requirements**. A penalty-only framework for quality-related criteria is in line with the precedent set by both the CAA's own capex engagement incentive for NERL under NR23² and Ofgem's RII0-3 BPI Stage A requirements³.

Please feel free to approach us with any questions on our response to this consultation.

Yours sincerely,

Rory Lillington
Networks & Alliances
British Airways Plc

² CAP2394b, Appendix G, paragraph G24

³ RII0-3 Business Plan Guidance